No. 3920

In The United States Circuit Court of Appeals

For The Ninth Circuit

FIDELITY AND DEPOSIT COMPANY OF MARYLAND, a corporation, and MARYLAND CASUALTY COMPANY, a corporation, *Appellants*,

vs.

KELSO STATE BANK, an insolvent banking corporation, and JOHN P. DUKE, as Supervisor of Banking of the State of Washington, in charge of and liquidating the assets of the KELSO STATE BANK, *Appellees.*

UPON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF OREGON

HON. R. S. BEAN, *District Judge.*

APPELLANTS' PETITION FOR REHEARING

MCCAMANT & THOMPSON,
Northwestern Bank Bldg., Portland, Ore., and
GRINSTEAD, LAUBE & LAUGHLIN,
314 Colman Bldg., Seattle, Washington,
Solicitors for Petitioners.

WALLACE MCCAMANT, Portland, Oregon and
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PETITION FOR REHEARING

Appelants earnestly request a rehearing herein.

Properly to hold with the appellees, this court must have found:

(1) That the County Treasurer's deposit

was validly received without knowledge of the Bank's officers of its insolvency; *or*

(2) That the moneys so deposited by the Treasurer were no traced into the warrants; *and*

(3) That the warrants were not pledged as collateral to secure the County Treasurer's deposits generally.

Upon the first point, relative to the knowledge of the Bank's officers of its admitted condition of insolvency at the time the deposit was received, the majority opinion quotes *conclusions* testified to by the Assistant Cashier (who could hardly be expected to admit criminal knowledge), and entirely ignores the pregnant facts. For instance, prior to receiving the deposit of March 14th, the Bank's President, Cashier and Assistant Cashier knew (but the Bank Commissioner, quoted in the majority opinion, did not yet know) that the *sole remaining chance of averting disaster had disappeared* (Exs. 19, 21). Surely this testimony is more potent than guarded expressions of conclusions made by the Assistant Cashier at the time of trial.

The majority opinion also holds that the Cashier's knowledge is not imputable to the Bank. We respectfully insist that such is not the law as laid down either in logic or in precedent but, assuming it to be correct, what about the knowledge of Mr. Carothers, the President, and Mr. Plamonden, the Assistant Cashier? Both of them knew, before they retired on the night of the 13th, that the last possi-

bility under which the Bank could continue had ceased to exist, and the Assistant Cashier, expressing the views of the President and himself (Plamonden is the son-in-law of Carothers) had written for the Bank Commissioner to come "the sooner the better."

Upon the second point, the majority opinion assumes that the Pope & Talbot draft was deposited as a general deposit in the United States National Bank, and asserts a failure to trace the County moneys into the warrants in question. Absolutely undisputed is the evidence to the contrary. The sole evidence is that the Pope & Talbot draft was taken to the note teller and there surrendered in redemption or repurchase of the warrants. This testimony is confirmed by the rubber stamp impression upon the check in evidence. The Pope & Talbot draft was never deposited or purported to be deposited in the Kelso Bank's account in the Portland Bank, nor was there any evidence that such conduct was intended.

The majority opinion concludes that the transaction between the two banks was a loan upon security of the warrants. What difference does it make to so construe the repurchase agreement? In either event, the Portland Bank held the warrants rightfully until it received a sum of money. It did receive it, in the Pope & Talbot draft. That deposit of the County Treasurer, being traced, entitles the Treasurer to all the rights of the Portland Bank, whether they be a title or lien in and to the war-

rants. The majority opinion augments the estate of the insolvent Bank by the fraudulent receipt of the deposit of the County Treasurer.

Upon the third point, the deposit of the warrants as collateral to indemnify the County Treasurer is dismissed, in the majority opinion, by a reference to the trial court's comment that the purpose of giving this collateral was to procure further deposits by the County Treasurer. The *sole* evidence is that of Mr. Tucker, to the effect that Mr. Stewart directed that the warrants be deposited in the Portland Bank's safe-keeping department as collateral security to the County Treasurer; and the receipt as issued by the U. S. National Bank.

We respectfully urge that, under these circumstances, the majority opinion is entirely unsatisfactory as a legal answer to the questions propounded.

As grounds for reconsideration, therefore, we urge:

I.

That the court has misconstrued the evidence and misapplied the law relative to the knowledge of the Bank's officers of its existing insolvency at the time of the County Treasurer's deposit.

II.

That the court has erred in holding that knowledge of the Cashier is not imputable to the Bank and has ignored the undisputed evidence that the President and Cashier, at the time of the deposit in question, knew positively of its hopeless condition.

III.

The court has erred in holding that the County Treasurer's deposit was not traced into the payment which released the warrants from the United States National Bank and, so failing, has misapplied the law.

IV.

The court has erred in ignoring the legal effect of the collateral receipt given by the United States National Bank and the deposit of the warrants with it, as security to the County Treasurer.

I.

KNOWLEDGE OF INSOLVENCY

On the night of March 13th, 1921, after the previous conferences and efforts to resuscitate the Bank, there met at the Bank at Kelso, Mr. Carothers, its President, Mr. Stewart, its Cashier, Mr. Plamonden, its Assistant Cashier, and Mr. L. N. Plamonden, the banker from Woodland. The purpose of that meeting was to ascertain whether it was possible to save the Bank. The two Plamondens were desirous of acquiring the Bank and financially able to do so but, in the early morning hours, before adjourning, they wrote to the Bank Commissioner the letter (Pltff's. Ex. No. 19) showing, not that it was impossible for them to acquire the Bank, but that the Bank's condition was such that no sensible person would undertake its resuscitation. Also Mr. George Plamonden wrote (Pltff's.

Ex. 21) the Bank Commissioner that Carothers, his brother and himself, were agreed on the Bank's condition. When, therefore, subsequently the Treasurer's deposit was received, the President and the Assistant Cashier already knew of the Bank's condition and the Bank Commissioner had been summoned. They were merely waiting for him to take charge, instead of taking the responsibility of closing the doors themselves. It matters not what actual or ostensible mental attitude Mr. Stewart had; the conduct and utterances of the parties at the time are more potent than George Plamonden's subsequent conclusions on the witness stand made with the criminal statutes staring him in the face and cited in the majority opinion.

Mr. Plamonden's testimony, however, was not confined to the isolated expression of opinion cited in the majority opinion. He said (R. p. 146):

> "That examination which we made showed that, in our estimation, there was a great deal of objectionable paper among the bills receivable of Kelso State Bank. We figured that there was somewhere around one hundred thousand dollars worth of paper that it was very questionable if collections could be made upon. We figured that there was something a little over one hundred thousand dollars that we figured would be paid, but that was most probably slow. In our estimation we considered it to be good, but we considered it to be slow. But of the parties who participated in that examina-

tion, *we did not all agree in these conclusions.* Mr. Stewart objected quite strenuously to a great many of our ideas. A large part of the paper that we thought was worthless in our opinion, Mr. Stewart insisted that in his opinion would eventually be paid. *It was largely a matter then of a difference of opinion. Mr. Carothers, I think, coincided with my brother and myself in those opinions; he thought there was one hundred thousand dollars of uncollectible paper.*"

The above quotation shows that the only officer of the Bank who even claimed to believe the Bank was solvent was the Cashier. The President of the Bank, the Assistant Cashier and the latter's brother, who was a banker at Woodland, believed there was at least one hundred thousand ($100,000.00) dollars of uncollectible paper in the bank and another one hundred thousand ($100,000.00) dollars of slow and doubtful paper. The subsequent facts showed that this belief was well founded, and it is submitted that the President and the Assistant Cashier of the Bank had no right to keep the Bank open and receive deposits when they believed that it was in the condition stated.

The majority opinion cites Plamonden as testifying that Stewart said, "We would come out all right." The opinion clearly infers that this was Stewart's opinion on the night of the 13th, after the examination was concluded. The record shows nothing of the sort. Plamonden testified, in sub-

stance, that, about a week or ten days before the Bank closed, Stewart came into the Bank looking so worried that he went back to Stewart at his desk and asked him, if the worst came to the worst, whether he was going to do anything rash. It was then that he testified that Stewart said, "Everything would come out all right." (R. pp. 147-150). This not only completely nullifies the force of that statement, as used in the majority opinion, but it also shows that Mr. Plamonden and Mr. Stewart, at *that* time, a week or ten days before, were mentally facing the problem of the Bank's impending failure, to the extent of discussing possible suicide. Brave words then uttered to build up false hopes or to avert suspicion have little potency as evidence of Stewart's true state of mind. Of far more probative value is Plamonden's mere statement that he saw that Stewart looked worried, to the extent that he thought it advisable to go back and try, if possible, to avert his suicide.

Let us not be diverted, however, from the fact that all of this occurred a week or ten days before the final decision on the last hope of averting disaster. Let us not forget that the knowledge that the Bank must fail was not solely Stewart's, but also Carother's and Plamonden's, and this was prior to the Treasurer's deposit of the 14th.

Even the Bank Commissioner, at the Chehalis meeting of March 6th, knew and stated that the Bank must close unless a one hundred per cent. assessment were levied and paid. He testified that,

when he found that the stockholders were unable to meet the assessment, *he concluded to close the Bank* (R. p. 134).

Further, relative to the examination of March 13th, he testified:

> "It was not entirely for the purpose of getting hold of Stewart's interest that this examination was made; it was a question of saving the Bank or preventing the closing of it." (R. p. 130-131).

Mr. Minchull, a Deputy Bank Examiner, testified to telling Stewart, in November, 1920, that he was "kidding" himself as to the value of the Bank's assets (R. p. 136). He further testified that, at the Chehalis meeting on March 6th, 1921, after Mr. Hay had advised the officers present that it was necessary to levy an assessment of one hundred per cent., Mr. Marsh, a *director of the Bank*, remarked, "that it would take all of that, or to the effect that there would not be enough." (R. p. 136). Between that date and March 13th, it had been determined that *the one hundred per cent. assessment could not be collected.* Under these circumstances, Mr. Marsh also knew, prior to March 14th, that the Bank could not survive.

What substantial justification, therefore, is there to rest the majority opinion on Mr. Plamonden's testimony that Mr. Stewart expressed himself optimistically? It does not prove that he was talking his convictions or knowledge, nor does it prove that the other officers, Carothers, Plamonden and Marsh

were of the same mind. In fact, the testimony is the other way and George Plamonden's letter of March 14th had summoned the Bank Commissioner (Pltff's. Ex. 21) to come "the sooner the better." What could it avail, unless the Commissioner closed the Bank (which he did)? Why the haste, unless it was to avert criminal responsibility?

Let us be candid. Assuming that every one connected with it knew that the Bank was hopelessly insolvent and bearing in mind Mr. Stewart's disappearance and probable suicide and the criminal statutes applicable to the other officers, just what would you expect us to be able to get by way of evidence that is not in this record? Do you expect us to have Mr. Carothers take the stand and testify that he left the Bank open after he had definitely determined that it was criminal to leave it open? Do you expect George Plamonden to take the stand and testify that the Bank remained open after he knew that it was hopelessly insolvent? Do not their acts, conversations and correspondence, at the time, show their feeling in the matter? Does not George Plamonden's letter show an intense desire on his part to have the Bank Commissioner take the responsibility? The letter states that his letter reflects Mr. Carother's views as well, and he wanted the Bank Commissioner there "the sooner the better."

Men engaged in crime are not accompanied by brass bands. George Plamonden's letter, however,

supplementing his brother's report, is about as striking.

The facts in the cases cited in the majority opinion as supporting the conclusion reached are entirely different from the facts in the instant case.

The distinction betwen the case of *Quinn vs. Earl*, 95 Fed. 728, and this case is so clearly pointed out in the dissenting opinion herein and in the appellants' brief that further comment is unnecessary.

In the case of *Brennan vs. Tillinghast*, 201 Fed. 609, Brennan had borrowed $1,000.00 from the bank on February 1st, 1909, executing his promissory note, payable in four months. On April 8th, 1909, he deposited $1,000.00 in the bank with the understanding that it was to be used in paying his note at maturity. On June 14th, 1909, he gave up his original intention of paying his note, paid the interest then due and gave a renewal note. The bank closed on June 21st, 1909. The court, in holding that he could not recover the $1,000.00, said:

> "In the present case it merely appears that the bank was insolvent at the time this deposit was received, and had been known to be insolvent for ten years previously by the cashier who received the deposit. The extent of its insolvency at that time is not shown, *nor is there any evidence as to what subsequent events precipitated the condition which caused its doors to close*, or whether or not at the time the deposit was received the bank, although embarrassed and insolvent, yet had reasonable

hopes that by continuing in business it might retrieve its fortunes, just as it had previously continued in business for the ten preceding years during which it had been insolvent. In the light of this meager evidence, we agree in the view expressed by Judge Denison, then district judge, who heard this case below, who said:

> 'There is no reason to think in this case that the suspension of the bank was any more imminent on April 8th than it had been for a long time, or that the cashier or bank officers anticipated the closing of the bank or had any expectation that complainant would not receive his money when he should ask for it—except their general and vague fear that they might fail to tide over their difficulties. This does not seem to me to raise the necessary trust. *Complainant's own showing is that for more than 60 days the deposit would have been repaid on demand, and that it was practically offered to complainant when the note was renewed.* For these reasons, I think complainant is not entitled to any preference upon his certificate of deposit, but should prove the same as a general creditor.'

And, whatever would have been the result otherwise, we think it cannot properly be held that the receipt of this particular deposit constituted a fraud upon Brennan within the rule

entitling him to follow it as a trust fund, in the light of the undisputed facts, shown by his own testimony that at the time the deposit was made the bank held his $1,000 note for borrowed money, and the deposit was made with the "understanding" that it would be used in payment of this note at maturity. *As this deposit was hence, under this evidence, in effect taken by the bank as quasi security for the payment of a just debt due to itself, this circumstance alone, in our opinion, relieves the bank from imputation of fraud in receiving the deposit, which might otherwise have existed if the deposit had been merely received in the ordinary course of dealings between the bank and a customer not indebted to it.*"

In the case of *Williams vs. Van Norden Trust Co.*, 93 N. Y. S. 821, the inventory and schedule filed after the assignment showed:

Debts and Liabilities	$54,497.81
Assets nominally worth	55,850.77
Assets actually worth	51,500.43
Deficiency	2,997.38

The testimony was that the firm was not in fact insolvent when the assignment was made and that the assets would have exceeded the liabilities if they had been properly handled.

In the case of *Furber vs. Dane*, 204 Mass. 412, the court stated that there was nothing to show that the members of the firm knew it was insolvent at the time of the transaction.

II.

Stewart's Knowledge Imputable to Bank.

The majority opinion states:

> "Nor was his (Stewart's) knowledge of his own mismanagement imputable to the officers of the Bank."

While Stewart's misjudgment, mismanagement and possible fraudulent conduct may be said to be the reason for it, the vital question is whether the Bank, at the time the deposit was received, had knowledge of its own insolvent condition. The knowledge of the officers is the knowledge of the Bank. We have already pointed out herein that the other officers and a director knew and appreciated its insolvent condition. However, Stewart's knowledge is imputable to the Bank.

He knew that, if the Bank was to continue, it was necessary for him to raise over ninety thousand dollars immediately (Ex. 19). He knew that he had defrauded the Bank of over fifty-five thousand dollars, an amount exceeding the sum of its capital and surplus (R. 107-8). He knew his own financial condition, which was that of absolute insolvency (R. 103). He therefore knew that he could not raise that which he must raise in order that the Bank should continue.

In support of their opinion, the majority cite *Perth-Amboy Gas Light Co. vs. Middlesex County Bank*, 60 N. J. Eq. 34, and quote from that decision as follows:

> "Of course, it almost goes without saying

> that the facts that the Cashier knew for months that the Bank was insolvent is not notice to the other officers of the Bank. It might as well be argued that the owner of a chattel, which has been stealthily stolen from him by his employee, is chargeable with notice of such theft and estopped from asserting his title to the stolen chattel when found."

In that case, the Cashier was not the managing officer; did not receive the deposit under consideration, but had previously absconded. In our case, appellees stressed the extent of Mr. Stewart's absolute control as managing officer of the Bank. He personally received the deposit and personally utilized the Pope & Talbot draft, received from the County Treasurer, at the Portland Bank. All transactions between the Kelso Bank and the County Treasurer and all transactions in question between the Kelso Bank and the Portland Bank were conducted by Mr. Stewart. In the transaction in question, Mr. Stewart was not engaged in defrauding the Bank which he managed, nor was he acting adversely to its interests. On the other hand, the transactions were for the benefit of the Bank and augmented its assets.

The cases holding that a bank or other corporation is not charged with the knowledge of its officer as to transactions in which the officer is acting adversely to its interest are not in point. This case is clearly within the rule that, when an officer, acting for or representing a corporation, is dealing

with a third person, all of the knowledge which the officer has, regardless of how he acquired such knowledge, is chargeable to the corporation.

This distinction is clearly pointed out in *Pennington vs. The Third National Bank of Columbus* (Va.), 77 S. E. 455, 45 L. R. A. (N. S.) 781. We quote from that case as follows:

> "The concrete proposition, upon the correct solution of which the decision must rest, involves the relation between a bank and its customer with respect to a deposit made by the latter in the following circumstances: At the time the cashier of the Bank of Tarboro received the draft in question for collection, and made the collection, he knew that the bank was hopelessly insolvent; but the depositor and the other officers of the bank had no knowledge of its insolvent condition. And the insolvency of the bank was due to the defalcations of the cashier and assistant cashier.
>
> "The authorities are agreed that when a bank, with knowledge of its insolvency, receives a deposit, it perpetrates a fraud on the customer, and is held to be a constructive trustee of the deposit, and the depositor may recover of the receiver the deposit, if it can be identified, or its equivalent, if it cannot be identified, when the customer's money has been mingled with the bank's funds, which, to an amount equal to the deposit, has gone into the hands of its receiver. *Western German Bank*

vs. Norvell, 69 C. C. A. 330, 134 Fed. 724; Tiffany, Banks and Bkg., Sec. 89, p. 349, and cases cited in notes.

"The correctness of the general principle is conceded; but it is said that this case falls within the exception to the doctrine of imputed knowledge (which doctrine is founded upon the presumption that an agent discloses his knowledge to his principal), because the fact that the insolvency of the bank was due to the defalcation of the cashier repels the presumption that he imparted the knowledge to the bank. *Baker vs. Berry Hill Mineral Springs Co.*, 112 Va. 280—L. R. A. (N. S.)—71 S. E. 626.

"We cannot agree that this case is controlled by the foregoing exception. The defalcations of the cashier and his assistant which caused the insolvency of the bank, occurred prior to the receipt and collection of the draft in question; and the transaction was not between him and the bank, but between him, acting for and representing the bank as its executive officer, and the bank's customer, the Georgia bank. Throughout the transaction, the cashier was acting for, and as the sole representative of, the bank, and in the line and within the scope of the powers and duties of his office with respect to the matter in hand; and therefore his knowledge of the insolvency of the bank (though brought about by his antecedent misconduct) was its knowledge. *In other words,*

the insolvency of the bank was a condition within the knowledge of its executive officer; and it matters not, so far as the rights of innocent third persons dealing with the bank through him are concerned, how he first acquired knowledge of that condition. *First Nat. Bank vs. Richmond Electric Co.*, 106 Va. 347, 7 L. R. A. (N. S.) 744, 117 Am. St. Rep. 1014, 56 S. E. 152; *Atlantic Trust & S. D. Co. vs. Union Trust & Title Co.*, 111 Va. 574, 579, 69 S. E. 975; Wade, Notice, 2d Ed. Secs. 683a, 683b; *Cook vs. American Tubing & Webbing Co.*, 28 R. I. 41, 9 L. R. A. (N. S.) 193, 211, 65 Atl. 641; *Morris vs. Georgia, Loan Sav. & Bkg. Co.*, 109 Ga. 12, 46 L. R. A. 506, 34 S. E. 378; *Bank of United States vs. Davis*, 2 Hill 451; *Holden vs. New York & E. Bank*, 72 N. Y. 286; *Le Duc vs. Moore*, 111 N. C. 516, 15 S. E. 888; *St. Louis & S. F. R. Co. vs. Johnston*, 133 U. S. 576, 33 L. Ed. 686, 10 Sup. Ct. Rep. 390; *Atlantic Cotton Mills vs. Indian Orchard Mills*, 147 Mass. 268, 9 Am. St. Rep. 698, 17 N. E. 496.

"In *Le Duc vs. Moore*, 111 N. C. 516, 15 S. E. 888, in an action by the receiver of a bank on a promissory note against the maker and payee, the latter being the president of the bank, to which he transferred the note by indorsement, the president and cashier constituted the discount committee and discounted the note. Held, that the bank took the note subject to equities

existing in favor of the maker at the time of the indorsement.

"In *St. Louis & S. F. R. Co. vs. Johnston*, 133 U. S. 576, 33 L. Ed. 686, 10 Sup. Ct. Rep. 390, the bank became insolvent by the operations of a firm of which the president of the bank was a member. A draft was deposited in the bank for collection. Held, that the knowledge of the president of the bank's insolvency, though occasioned by his firm, was the knowledge of the bank.

"In the leading case of *Atlantic Cotton Mills vs. Indian Orchard Mills*, 147 Mass. 268, 9 Am. St. Rep. 698, 17 N. E. 496, Gray was the common treasurer of two corporations; and, in order to make good his deficit in one of the crporations, he drew checks upon the other payable to the order of the first, by which the money was drawn and used; no other officer of either corporation knowing the facts. A similar contention was made in that case as in this—that knowledge of the officer could not be imputed to the corporation. But the court, at page 273, says: 'It is true that no officer of the plaintiff, besides Gray, knew of the fraudulent origin of these checks; but, in the very transaction of receiving them, the plaintiff was represented by Gray, and by him alone, and is bound by his knowledge. It is the same as if the plaintiff's directors had received the checks, knowing what he knew.

For the purpose of accepting the checks, Gray stood in the place of the plaintiff, and was the plaintiff. It is quite immaterial, in reference to this question, in what manner or by what officers of the corporation the funds were afterwards used.'

"In the course of the same opinion, at page 276 of 147 Mass., Judge Allen observes: 'We have preferred to put the decision of this point upon the broad ground that, if the treasurer of a corporation is a defaulter, and his defalcation is as yet unknown and unsuspected, and he steals money from a third person, and places it with the funds of the corporation in order to conceal and make good his defalcation, and the corporation uses the money as its own, no other officer knowing any of the facts, the corporation does not thereby acquire a good title to the money as against the true owner, but the latter may maintain an action against the corporation to recover back the same.' "

The foregoing rule is recognized in the *Perth-Amboy G. L. Co.* case, relied on by the majority opinion. In that case, the court stated the rule to be that the depositor, in order to recover, must show that the officers of the bank who transacted the business with him, knew of the insolvent condition of the bank at the time they accepted the deposit.

In the case of *Tatum vs. Commercial Bank and Trust Co.* (Ala.), 69 S. 508, L. R .A. 1916 C, 767,

774, the distinction between cases like the *Perth-Amboy* case and the instant case is clearly pointed out, and a great number of authorities are cited. After stating the general rule that a corporation is chargeable with the knowledge of its officers or agents and the exception that, if the officer or agent has an individual interest in the matter adverse to the corporation, the corporation is not so charged, the court states that this exception has a qualification or limitation as to cases like the one on trial, that is, where the corporation has no other agency or representative in the matter and where the party asserting the knowledge or notice on the part of the corporation is guilty of no negligence or fault in the transaction. After reviewing the cases, the court sums up the rule as follows:

> "The authorities, therefore, lend support to two qualifications applied in *Bookhouse vs. Union Publishing Co.*
>
> "1. That the exception does not apply when the officer of the corporation, though he acts for himself or a third person, is also the sole representative of the corporation in the transaction. This qualification, as applied by the cases is not at all dependent upon the question whether or not the corporation would be benefitted by the transaction as a whole, if the knowledge possessed by its officer were held not to be chargeable to it.
>
> "2. *That the exception does not apply where the corporation, even if it were held not to be*

chargeable with notice of the fraud of its officer, would, as a result of the whole transaction, be in a better position."

In the instant case, the appellees, while denying that the cashier's knowledge is imputable to the Bank, seek to retain the benefits of the transaction between the Bank, acting through the cashier, and the county treasurer.

To hold that the appellants are not entitled to recover is to permit the bank and the general creditors to keep over Thirty-five Thousand ($35,000.00) Dollars which they would not have received if the Bank's agent, Mr. Stewart, had not permitted the deposit by the county treasurer.

With the facts as they are shown by the record in this case and the law as announced in the majority opinion, an officer of a corporation can defraud a third party out of money for the benefit of his corporation and the corporation can retain the proceeds of the fraud and defend on the ground that it is not chargeable with the knowledge of its officer.

Such a rule is contrary to the well established principle of law that a person cannot receive the benefits of a transaction and at the same time disclaim responsibility for the measures by which they were acquired.

21 R. C. L. 932, and cases cited.

Atlantic Mills vs. Indian Orchard Mills, 147 Mass. 268; 9 Am. St. Rep. 698.

Furthermore, the doctrine announced in this case

to the effect that the Bank is not chargeable with the knowledge of its Cashier is contrary to the rule established by the Supreme Court of the United States in the case of *St. Louis & S. F. R. Co. vs. Johnston*, 133 U. S. 576, and cases cited therein.

The Supreme Court of the State of Washington, in the case of *Raynor vs. Scandinavian-American Bank*, 22 Wash. Dec. 46 (decided Nov. 3, 1922), quoted with approval from the case last above cited as follows:

> "This bank was hopelessly insolvent when the deposit was made, made so apparently by the operations of a firm of which the President of the bank was a member. *The knowledge of the President was the knowledge of the bank. Martin vs. Webb*, 110 U. S. 715; *Banks vs. Walker*, 130 U. S. 267; *Cragie vs. Hadley*, 99 N. Y. 131."

III.

The Treasurer's Deposit Is Traced Into the Warrants.

The evidence of Mr. Tucker, Vice-President of the United States National Bank, is that Mr. Stewart brought the Pope & Talbot draft to the Portland Bank, after closing hours; stated that he had come for the purpose of procuring the warrants; took the draft to the note teller's cage and received the warrants; that he then directed the deposit of the warrants so procured as collateral security to the County Treasurer and directed that the receipt

should be mailed to the Treasurer; and that *subsequently*, after Mr. Stewart had departed, as a matter of convenience in bookkeeping, the whole amount received by the note teller was credited to the Kelso Bank's account and a debit, for the amount due on the warrants, was charged to that account; that Mr. Stewart made no deposit and that he drew no check against the Kelso Bank's account (R. 162-175).

This testimony is absolutely uncontradicted and, under the rule cited in the majority opinion, this court cannot find to the contrary.

However, even if the money had been deposited by the Kelso Bank, as a general deposit, and a check drawn against it to pay for the warrants, the legal presumption would be that it was the trust funds which were used to obtain the warrants.

Brennan vs. Tillinghast, 201 Fed. 609 (614).

In the above case, the court cited the rule as follows:

> "It is true that in the case of blended moneys in a bank account, consisting in part of trust funds, from which there have been drawings from time to time, it has been held, in favor of the *cestui que trust*, as a presumption of law, that the sums first drawn out were from the moneys which the tort-feasor had a right to expend in his own business, and that the balance which remained included the trust fund, which he had no right to use. In re *Hallett's Estate*, 13 Ch. D. 696, 727; *Board of*

Commissioners vs. Strawn, supra, at page 51. It is clear, however, in the first place, that this is a mere presumption, which will not stand against evidence to the contrary. *Board of Commissioners vs. Strawn, supra,* at page 51.

"And it is furthermore clear that *this rule of presumption has no application where the evidence shows that the first moneys drawn out of the mingled fund by the tort-feasor were not in fact dissipated by him at all, but were merely transferred, in a substituted form, to another fund retained in his own possession. In such case, it must be held that the trust attaches to the substituted form in which the property is retained by the tort-feasor, and that the right to follow the trust in such form is not lost by reason of the fact that the tort-feasor thereafter draws out and spends for his own purposes the balance of the fund in which the trust money was originally mingled.* The English case of *In re Oatway,* L. R. 2 Ch. 356, 359, directly sustains this view. In that case Oatway, a joint trustee under a will, had sold a portion of the trust property and deposited the proceeds to his own credit in bank with other funds belonging to himself. Out of this deposit, consisting in part of the proceeds of the converted trust fund and in part of his own moneys, Oatway purchased certain shares of stock in the Oceana Company, which he took and retained in his own name. Thereafter he

drew out and paid away irrevocably for his own individual purposes the entire remainder of the bank deposit. It was held that, under this state of facts, the *cestui que trust* was entitled to follow the shares of stock thus purchased by Oatway. Joyce, J., said:

> " 'If money held by any person in a fiduciary capacity be paid into his own banking account, it may be followed by the equitable owner, who, as against the trustee, will have a charge for what belongs to him upon the balance to the credit of the account. If, then, the trustee pays in further sums, and from time to time draws out moneys by checks, but leaves a balance to the credit of the account, it is settled that he is not entitled to * * * maintain that the sums which have been drawn out and paid away so as to be incapable of being recovered represented *pro tanto* the trust money, and that the balance remaining is not trust money, but represents only his own money paid into the account. * * * *It is, in my opinion, equally clear that when any of the money drawn out has been invested, and the investment remains in the name or under the control of the trustee, the rest of the balance having been afterwards dissipated by him, he cannot maintain that the investment which remains represents his own money alone, and that what has been spent and can*

no longer be traced and recovered was the money belonging to the trust. * * * The order of priority in which the various withdrawals and investments may have been respectively made is wholly immaterial. * * * In the present case there is no balance left. The only investment or property remaining which represents any part of the mixed money paid into the banking account is the Oceana shares purchased for £2,137. Upon these, therefore, the trust had a charge for the £3,000 trust money paid into the account. That is to say, those shares and the proceeds thereof belong to the trust. The investment by Oatway, in his own name, of the £2,137 in Oceana shares no more got rid of the claim or charge of the trust upon the money so invested than would have been the case if he had drawn a check for £2,137 and simply placed and retained the amount in a drawer without further disposing of the money in any way. The proceeds of the Oceana shares must be held to belong to the trust funds under the will of which Oatway and Maxwell Skipper were the trustees.'

"In like manner we are of opinion that in the present case it must be held that the transfer by the Ironwood Bank to its own vaults, through the cash draft transactions, of $2,-807.32, of the balance standing to its credit

in the Duluth Bank in which the trust fund had been mingled, did not divest the money thus transferred of its character as a trust fund, but as this money remained thereafter in its own vaults and in its own custody, and subsequently passed into the hands of the receiver as part of the cash assets of the bank, it remained subject in all respects to the trust originally impressed upon the proceeds of the sale of Brennan's stock."

The majority opinion suggests the rule that, where trust moneys are used to pay the debt of an insolvent, the insolvent estate not being benefited, the trust is dissipated. That rule is inapplicable here because the debt paid (granting that it was the payment of a debt) was a secured debt and the effect of the payment was to release assets into the insolvent Bank's estate.

It matters not, therefore, whether the transaction is construed to be either a purchase, under the repurchase agreement literally construed, or the payment of a loan. If it was a purchase, the Treasurer's money bought the warrants. If it was the payment of a loan, the Treasurer's money (paying the loan) became equitably entitled to the security which protected that loan.

In either event, the Treasurer's money enriched the insolvent's estate. If the Treasurer's money had not been turned into the Portland Bank, then

the appellees, to recover the warrants, must pay the Portland Bank in full; whereas, under the majority's ruling, they take the warrants without paying the Portland Bank or any one else any sum whatever, thereby enhancing the insolvent estate to the extent of $32,897.97, the amount of the Pope & Talbot draft.

Under the well established rule so recently announced by the Supreme Court of the State of Washington, in the case of *Raynor vs. Scandinavian-American Bank* (decided Nov. 3rd, 1922, 22 Wash. Decs. 46), it is only necessary to show that the gross assets of the Bank have been augmented by the deposit which it sought to recover. In other words, all that the Kelso Bank's creditors can ask is that they receive the same amount that they would have received if the deposit and subsequent transactions had never occurred.

IV.

The Warrants Pledged Apply in Protection of Past, as Well as Contemplated Future, Deposits.

Mr. Tucker testified that Mr. Stewart directed the deposit of the warrants for safe-keeping as security for deposits of County funds, and that the collateral receipt should be sent to the County Treasurer (R. 165); that he (Tucker) placed the warrants in the Portland Bank's safe-keeping department, and instructed the issuance of the receipt

(R. 170). The receipt is in evidence (Ex. 31). That was the transaction which took place. We neither evade nor dispute that Mr. Stewart had in mind that the County Treasurer would thereby be enabled to deposit more moneys, but in no testimony is there ever shown any arrangement or suggestion that the collateral security was limited, in its application, to future deposits. The written evidence and Mr. Tucker's testimony of Mr. Stewart's oral instructions are entirely devoid of any such suggestion. The intention of the parties, as gleaned from the uncontradicted testimony, was that all securities available to the County Treasurer were to cover all of his deposits, past and future.

Mr. Brown testified that Stewart sent Plamonden seeking more of the County's deposits and his answer was, "That, if he would put up the security, he would possibly get the deposits" (R. p. 177).

We repeat again that *the record is absolutely devoid of testimony that the warrants were pledged to secure the Treasurer as to subsequent deposits only.* The pre-existing indebtedness was a sufficient consideration to support the pledge. We feel that, on this subject at least, appellants' brief (pp. 34-41) is adequate and conclusive, and that therefore the majority has failed to get the true analysis and purport of the record.

We feel that somehow we have failed to convey to the majority of the court the true importance, significance, import and legal effect of the salient

features of the testimony in this case. We humbly suggest that the majority opinion is not worthy of this high court. We are convinced that the fault must be our own. But fault there is—of that we are firmly convinced.

The amount involved herein is not inconsequential. Of greater and more lasting importance, however, is the proper application of legal principles. An erroneous declaration of a legal principle, or its misapplication, by a court of last resort, is a harm that time will not heal; it but intensifies the wrong. Under our judicial system, a bad precedent, or judgment ill pronounced, does not die with its pronouncement, but lives to touch and tarnish the entire current of the law.

We sincerely feel that justice will be accomplished more surely if we shall be permitted again to trespass upon the courtesy of the court. If our present convictions are erroneous, a rehearing will have cost little and make certain that fact. If, through our fault, the court has erred, a rehearing will correct that error by doing justice not only to our present clients, but to future litigations and to this court itself.

Respectfully submitted,

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WALLACE McCAMANT and
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Of Counsel.

I hereby certify that, in my judgment, the foregoing petition for rehearing is well founded in law; and is not made, nor interposed, for delay.

LOREN GRINSTEAD,

Solicitor for Petitioner.